



IBA Review of the Mayor's Five-Year Financial Outlook for FY 2012-2016

Meeting of the City Council
February 14, 2011



Overview

- Mayor's Five-Year Outlook for FY 2012-2016 is 5th update in series of long-term outlooks
- Presented to the Budget Committee on 2/9
- Committee forwarded to City Council with requests for additional information from Financial Management and IBA



Overview

- Budget Committee requested FM to:
 - Adjust Outlook to include Ballpark Debt transfer and other budget corrections
 - Provide details on new facilities (with associated costs and FTEs)
 - Provide explanation on how facilities were selected
 - Estimate impacts of fiscal reforms, department consolidations, organizational flattening and service reductions



Overview

- Budget Committee requested IBA to:
 - Develop a more candid and complete assessment, including:
 - calculation of the deferred maintenance deficit
 - incorporation of vacancy factor and step increases
 - unfunded portion of the Main Library project
 - additional details as identified in IBA presentation
- IBA Outlook Scenario addresses these issues and will be shown at end of this presentation



Overview

- Mayor is committed to bringing the Five-Year Outlook into balance by FY 2013
- Status of ten fiscal reforms provided
- Not all reforms can be completed in time to achieve deficit reduction for FY 2012 budget
- Some Council priorities not addressed



Overview

- IBA review and analysis typically relies on comparisons with prior year actual results, and current year projections
- Neither were available during the review; should be forthcoming in the weeks ahead
- Unavailability of this data hampered review and reasonableness checks



State Budget Impacts

- Outlook notes elimination of redevelopment agencies could have negative impact on General Fund by eliminating tax-sharing agreements and discouraging investment that could strengthen sales tax and TOT
- Outlook does not address possible positive impacts to General Fund due to allocation of tax increment revenues back to local agencies beginning in FY 2013



State Budget Impacts

- IBA will work with Financial Management to determine the potential increase in property tax revenues to City as more details of the Governor's proposal become available
- If tax extensions proposed by the Governor are not approved by voters, State funding for public safety grants could be eliminated; approx loss of \$1.65 million for Police Department



General Fund Revenue

- Given available data and current economic indicators and forecasts, most projections are appropriate
- Concern regarding Property Tax
- Highlight other large revenue changes



Property Tax

- Varying factors will impact Property Tax, leading to possible negative growth in FY 2012, and slower than forecasted recovery in outer years
- The “pessimistic” forecast for Property Tax may be more appropriate
- Using this, deficit could increase by \$3.8 million in FY 2012, and additional \$21 million in FY 2016; reflected in IBA Outlook Scenario



Sales Tax

- Sales Tax current performance exceeding projections thus far in the fiscal year
- Current base year projection for sales tax reflects 2.0% growth over previous year performance for the remainder of the fiscal year; most recent quarter receipts demonstrate growth of 4.3% over prior year (reflecting sales activity July –September 2010)



Fines, Forfeitures and Penalties

- In November 2010, Council authorized increase in parking citation fees for State-mandated surcharges previously paid by General Fund
- Estimated to save General Fund \$1.75 million in FY 2011 mid-year, and \$3.5 million in FY 2012 and beyond
- Now reduced to \$3.2 million annually; under review by Police Department



Interest Earnings

- Interest earnings projected to grow by 360% from \$1.7 million in FY 2012 to \$6.1 million in FY 2014
- Increase based on expected recovery of financial markets and anticipation that yields will increase to historical long-term average over next few years
- Reasonable to expect interest earnings will increase as pool becomes reinvested at higher rates (Yield on pooled assets fell to approx 1% in Dec 2010)



General Fund Expenditures

- Expenditures increase \$81.8 million over five year period
- Largest area of increase is Retirement/Pension of \$63 million (over 77% of total)
- Next largest increase is due to two planned bond issuances for deferred capital projects (\$14.8 million) in the Other category



Salaries & Wages

- No salary increases or restoral of 6% reduction for next five years; potential increases shown in IBA Outlook scenario
- Vacancy Savings – no longer separate line item
 - Adjusted \$1.7 million to correct 2011 amount
 - Cannot evaluate with limited information
- Annual Leave Liability
 - Estimated costs for accrued leave as employees depart City; significantly reduced from \$16 million to \$6.3 million in FY 2014



Pension

- June 30, 2010 UAL is \$2.15 billion
 - Up from \$2.11 billion at June 30, 2009
- FY 2012 ARC estimated at \$231.2 million
 - Increase of \$2.1 million from \$229.1 million in FY 2011
 - General Fund contribution of \$179.2 million, up \$1.6M
- Reduction of \$21.2 million for FY 2012 since prior Outlook for General Fund



OPEB – Retiree Health

- According to the City's Budget Policy, the Outlook should "include the following amounts for each of the forecast's five years for retiree health care: the Annual Required Contribution (ARC); pay-as-you-go costs; and the unfunded liability, based on the following two scenarios:
 1. Based on current funding strategy of pay-as-you-go amount plus some additional amount for pre-funding future liability for retiree health (lower than the ARC).
 2. Based on payment of the full ARC each year."



OPEB – Retiree Health

- City is preparing for negotiations with all labor unions regarding the appropriate level of retiree health benefits
- It is anticipated that there will be an agreement on a new benefit level to be effective July 1, 2011
- \$57.8 million has been included for each year of the Outlook, matching FY 2011 amount



OPEB – Retiree Health

- Payment of the full Annual Required Contribution (ARC) for retiree health care costs is not legally required
- Guiding Principle #10 calls for a plan to fully fund the Retiree Health Care ARC
- Additional amounts needed for full ARC without reforms:

	<u>City-wide</u>	<u>General Fund</u>
FY 2012 OPEB ARC without reforms:	\$98.5 million	\$68.5 million
Current Amount in Outlook:	<u>\$57.8 million</u>	<u>\$40.2 million</u>
Additional needed to fund ARC	\$40.7 million	\$28.3 million



OPEB – Retiree Health

- Inclusion of the additional funding need of \$28.3 million for payment of full ARC without reform would bring the FY 2012 General Fund deficit to \$85.0 million
- Retiree health care reform key to permanently lowering annual retiree health care costs
- IBA Outlook Scenario shows full funding of Retiree Health Care ARC without reform



Non-Personnel Expenditures

- **Supplies; Contracts; Information Technology**
 - 0% annual growth for these categories
 - Includes \$ for elections, removal of one-times
 - No savings estimated for IT competition
- Though not described, funding for Community Plan Updates has been increased from \$800K annually to:
 - \$1.2 million in FY2012
 - \$2.8 million in FY2013
 - \$2.15 million in FY2014
 - \$250K in FY2015



Non-Personnel Expenditures

- Energy & Utilities – 5% growth
– Consistent with prior Outlooks
- “Other” category includes transfers, debt payments; this includes Mission Bay Lease Revenues, some transfers to Reserves



Reserves

- Outlook includes funding to meet reserve policy goals, consistent with revised policy currently awaiting approval
- Total of \$14.1 million required in FY 2012, declining to \$12.0 million in FY 2016
- General Fund policy goal to reach 8% by FY 2013; Public Liability & Workers' Comp. policy goal to reach 50% of claims by FY 2014



New Facilities

- List not provided in Outlook as in past, though requested by Budget Committee
- In response to questions, IBA learned:
 - Various Park and Recreation locations coming on-line in each fiscal year, including:
 - W Lewis & Falcon St
 - Linda Vista Terrace
 - Del Mar Mesa
 - Treena Mesa
 - Pacific Breezes Community Park
 - Bayside Fire Station starting in FY 2013



New Facilities - Main Library

- No changes since last version
- Scheduled to open in FY 2014
- Outlook assumes no net General Fund impact
- Additional operating costs anticipated to be offset with private donations and new revenue
- In IBA Outlook Scenario – unknown \$



Storm Water Compliance

- Outlook includes \$35.2 million per year for Storm Water compliance
 - No increase from FY11 Budget; expect to comply with current Municipal Permit
- New permit to become effective during Outlook may result in additional regulations
- Staff indicated during last budget review that Cost of Service Study was underway; results were expected in December 2010



Fire-Rescue Restorations

- At the January 26, 2010 PS&NS Committee meeting, Mayor's Office indicated there are no plans to restore rolling brownouts in FY 2011
- For FY 2012 and beyond, Mayor's Office working with Fire-Rescue Department on strategy to phase-in the restoration of overtime
- Details of phase-in not yet available



Fire-Rescue Restorations

- FY 2011 reduction due to rolling brownouts was \$11.5 million total
- Full-year restoration of each browned-out engine company requires \$1.4 million
- Council priority not addressed in Outlook
- Phase-in option shown in IBA Outlook Scenario; 2 engines added in FY 2012; 4 in FY 2013; 8 in FY 2014



Civic Center

- Prior Outlook included specific line item of \$5.5 million for CAB Fire Sprinklers, and described four scenarios for Civic Center:
 - Two for new construction; two for continued occupancy
- CAB Sprinklers funding eliminated in FY 2011
- CAB needs and Civic Center plans not explicitly addressed in new Outlook



Civic Center

- At 2/7 Council meeting, COO indicated:
 - Civic Center project no longer being pursued
 - CAB sprinklers are planned to come forward for Council action in Fall 2011
 - Funding for CAB sprinklers of \$4 million will come from bond proceeds for deferred capital
- Previous Outlook indicated that sprinkler costs not eligible for deferred capital bonds
- City Hall needs shown in IBA Outlook Scenario in FY 2012 and FY 2013



Deferred Capital

- Outlook includes debt service payments for the first March 2009 issuance; proposes two additional \$100 million issuances in FYs 2012 and 2015
- Prior Five-Year Outlook projected two additional bond issuances in FYs 2011 and 2013; bond issuances now postponed
- IBA Outlook Scenario shows cost impact of original schedule with no delays



Deferred Capital

- Current backlog of deferred capital/infrastructure projects is still estimated to be \$800-\$900 million
- Long-term plan to address full backlog is not discussed in Outlook
- Not yet in line with Guiding Principle #11 which calls for plan to fund needs to reduce backlog and adequately fund capital needs



Deferred Capital

- During FY 2011 Budget Review, staff estimated “catch-up” funding to a “high level of service” for Streets, Facilities, and Storm Drains would require \$564 million
- Funding is also required for “On-Going” maintenance of City’s Capital assets at a specified level
- IBA Outlook Scenario shows one option for cash funding “catch-up” funding



Deferred Capital

- IBA review of FY2011 Proposed Budget, staff estimated current budget includes \$86.9 million for the maintenance of the three main asset classes (Streets, Facilities, and Storm Drains)
- FY 2011 funding for Streets not sufficient to prevent backlog from increasing; other assets may have same situation
- Once policy is developed, Outlook should reflect annual requirements



Potential Solutions

- Managed Competition
 - May result in savings over Outlook period
- Pension & Benefit Reforms
 - Significant potential savings
- New Revenues
 - Previously discussed, but little political support; require voter approval
- User Fee Reviews and Adjustments
 - Status uncertain; potential for Police/Fire fees



Potential Solutions

- Third Amendment to Ballpark Cooperation Agreement approved by City Council and Redevelopment Agency on February 8, 2011 will mitigate \$11.3 million annually in Fiscal Years 2014, 2015 and 2016
- Agreement will extend until 2032
- Budget Committee requested Outlook be revised to reflect this action and adjustment to deficit in affected years



Conclusion

- Many past actions have been taken to move City toward financial health
- Without these accomplishments, fiscal challenges would be even more daunting
- Largely concur with Outlook projections
- Additional detail and actual prior year results needed to review properly



Conclusion

- **Mayor's Five Year Outlook for FY 2012-2016:**
 - Does not reflect possible “pessimistic” property tax outlook
 - Does not assume any increases in service levels
 - Does not include any restoration of Fire-Rescue rolling brownouts
 - Assumes retiree health care reform to reduce costs, or continuing practice of not paying full ARC for retiree health
 - Assumes no salary increases for five years
 - Assumes City Hall improvement needs will be funded from deferred capital bonds
 - Assumes receipt of library donations for Main Library
- IBA Outlook Scenario reflects estimate of annual deficit incorporating these important areas; may reflect a more accurate assessment of the City's financial situation



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General Fund - IBA Outlook Scenario					
(in millions)					
	FY 2012 Forecast	FY 2013 Forecast	FY 2014 Forecast	FY 2015 Forecast	FY 2016 Forecast
Five-Year Outlook Projected Deficit	\$ (56.7)	\$ (61.9)	\$ (54.9)	\$ (33.1)	\$ (8.8)
Ballpark Debt (TOT)	\$ -	\$ -	\$ 11.3	\$ 11.3	\$ 11.3
Five-Year Outlook Adjusted Deficit	\$ (56.7)	\$ (61.9)	\$ (43.6)	\$ (21.8)	\$ 2.5
Revenue Scenarios					
Property Tax (pessimistic)	\$ (3.8)	\$ (7.7)	\$ (11.9)	\$ (16.3)	\$ (21.0)
Five-Year Outlook Adjusted Deficit	\$ (60.5)	\$ (69.6)	\$ (55.5)	\$ (38.1)	\$ (18.5)
Expenditure Scenarios					
Salary Increases (2% 2013 and 2% 2015)	\$ -	\$ (10.0)	\$ (10.0)	\$ (20.8)	\$ (20.8)
Retiree Health Care Payment of Full ARC w/o reform	\$ (28.3)	\$ (28.3)	\$ (28.3)	\$ (28.3)	\$ (28.3)
Fire-Rescue Restorations (2, 4, 8 engines)	\$ (2.8)	\$ (5.6)	\$ (11.5)	\$ (11.5)	\$ (11.5)
City Hall Critical Deficiencies	\$ (4.2)	\$ (15.3)	\$ -	\$ -	\$ -
Subtotal:	\$ (95.8)	\$ (128.8)	\$ (105.3)	\$ (98.7)	\$ (79.1)



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General Fund - IBA Outlook Scenario					
(in millions)					
Additional Needs	FY 2012 Forecast	FY 2013 Forecast	FY 2014 Forecast	FY 2015 Forecast	FY 2016 Forecast
"Catch-Up" Funding for Three Main Asset Classes	\$ (72.6)	\$ (72.6)	\$ (72.6)	\$ (72.6)	\$ (72.6)
"Ongoing" Funding Deferred Capital	<i>unknown</i>	<i>unknown</i>	<i>unknown</i>	<i>unknown</i>	<i>unknown</i>
Initial Payments for Original Schedule for Deferred Capital Bonds	\$ (7.4)	\$ -	\$ (7.4)	\$ (7.4)	\$ -
Main Library Donation Shortfall	<i>unknown</i>	<i>unknown</i>	<i>unknown</i>	<i>unknown</i>	<i>unknown</i>
Additional Needs:	\$ (80.0)	\$ (72.6)	\$ (80.0)	\$ (80.0)	\$ (72.6)

"Catch-Up" Funding assumes cash funding over five year period the remaining needs, after two \$100 million bond issuances. (\$563 million less \$200 million = \$363 million.) Three main asset classes includes streets, facilities and storm drains.



Conclusion

- Few viable budget solutions available other than deep budget reductions and service cuts
- Reforms will assist in elimination of long-term structural deficit



Conclusion

- Council adopted eleven Guiding Principles for Structural Budget Deficit Elimination in February 2010
- Principle #4 states *“prepare a 5-year Outlook each year and provide numeric values for alternative budget balancing options based on input from City Council, Mayor and IBA; be prepared each year to discuss alternative budget balancing options with the Budget Committee or City Council should the Outlook suggest an ongoing structural deficit.”*



Conclusion

- The City Council may wish to discuss reasonable requests to be made of the Mayor to incorporate specific budget balancing options in the Five-Year Outlook, as agreed to in the Guiding Principles, and request presentation at future meeting